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BRAZIL: **Growing Tension With Creditors**

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Brazil's uncooperative attitude toward its creditors is setting the stage for a financial confrontation that will result in additional economic costs for both sides. [redacted] 25X1 25X1

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Some major US banks are considering reclassifying their loans to Brazil as nonperforming, according to press reports, in the wake of Brasilia's continued inflexible approach to its creditor banks. [redacted] 25X1 25X1

Comment: Brazil is unlikely to secure a formal agreement to renew its short-term credits by 31 March. These credits probably will decline despite the freeze and impede Brazil's ability to conduct trade. If banks refuse to provide new funding to Brazilian bank subsidiaries overseas, some of these institutions could come under serious pressure, with unknown consequences for international capital markets early next month. [redacted] 25X1

A continuing impasse with Brasilia may cause its US creditors to place Brazilian loans in a nonperforming status even before mandated by banking regulations. In addition, it would further erode business confidence in Brazil. The growing uncertainty probably will cause the private sector to postpone investment decisions and result in a decline of foreign investment. These factors, combined with stringent import licensing restrictions forced by reduced trade financing, probably will lead to a sharp drop in industrial production and employment within the next few months. [redacted] 25X1

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Top Exporters of Textiles and Apparel to the US, 1985

Billion US $

Taiwan	4.8
South Korea	4.0
Hong Kong	3.8
Italy	2.2
China	1.5
Brazil	1.2
Japan	1.3
Philippines	0.5
Spain	0.5

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THIRD WORLD: Reactions to Proposed US Textile Legislation

[redacted]

LDC fears of a resurgence of US protectionism have been aroused by the draft Textile and Apparel Trade Act of 1987. Hong Kong, South Korea, and Taiwan, claiming the bill would roll back their textile and apparel exports by at least 35 percent, are threatening unspecified retaliatory measures. Hong Kong says enactment would constitute a US abandonment of the Multifiber Arrangement and all bilateral agreements. South Korean trade officials denounced the bill as more severe than its predecessor. Taiwan stated the bill is particularly unfair in view of its recent initiatives to open its markets and to comply with US requests on issues of intellectual property rights. The reactions of India and Egypt have been far less critical. [redacted] New Delhi is urging its textile manufacturers to raise sales to the US under a new US-India bilateral agreement. Egypt asked the US not to apply the new restrictions to certain cotton textile shipments last year above quota limits until consultations between the two countries are completed. [redacted] 25X1 25X1 25X1 25X1

Comment: Indonesia, Malaysia, and Pakistan, which have yet to reach bilateral textile agreements with the US, are also likely to react unfavorably in bilateral negotiations. [redacted] 25X1

IRAN–SAUDI ARABIA: Tehran Sends Warning

[redacted]

Tehran is again pressuring Saudi Arabia to reduce its support for Iraq. According to press reports [redacted] an Iranian naval ship fired a rocket last Wednesday at a Saudi supertanker off the coast of Dubai. The rocket missed, but the incident marked the first attack by Iran against a Saudi ship since last May. [redacted] 25X1 25X1 25X1 25X1

Comment: Iran's actions may have been prompted by reports that the Saudis have agreed to allow Baghdad to increase the flow of Iraqi oil through the Iraqi-Saudi pipeline [redacted] Riyadh is unlikely to reduce its support for Iraq, but the Saudis will probably make some effort to mollify Tehran. [redacted] 25X1 25X1 25X1 25X1

TUNISIA-LIBYA: Gradually Improving Ties

The well-publicized visit of a senior Libyan security official to Tunis last week marks further progress in the normalization of relations between the two countries. The travel of a Tunisian delegation to Libya earlier this year led to an agreement in principle to open consulates and to Tripoli's release of some Tunisian financial assets frozen after the break in formal relations in 1985. ~~The US defense attache in Tunis reports Tunisia is refurbishing the customs offices on the Tunisian-Libyan border~~ 25X1

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Comment: The security official's visit is the most publicized contact in several years and follows secret talks between the two countries in Algiers late last year. A resumption of diplomatic relations is likely to take time, however, because of probable delays in Tripoli's payment of outstanding debts and compensation for the 30,000 Tunisian workers it expelled in 1985. 25X1

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BELGIUM-US: Visit of Vice Prime Minister

Belgian Vice Prime Minister Jean Gol visits Washington this week in his capacity as chairman of the EC counterterrorism group. He will sign a US-Belgian extradition treaty and hold discussions on counterterrorism with US officials. 25X1

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Comment: Gol is the most powerful member of the second-largest party in the Belgian ruling coalition and would like to become foreign minister. A successful term as chairman of the EC counterterrorism group—the Trevi Group—would restore his domestic political fortunes, which have been in decline recently because of the failure of Belgian security forces—for which he is responsible—to cope adequately with increased criminal and terrorist activities. 25X1

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TAIWAN-US: Anger Over Currency Appreciation

Currency revaluation has become a heated political issue in Taiwan in recent months; local media are accusing the US of pressing Taipei to revalue the New Taiwan dollar at 28 to the US dollar. In 1984, the rate was 40 to the US dollar; it is currently 35 to the dollar. The Council for Economic Planning and Development has warned that such a revaluation would force some local industries into bankruptcy as foreign remittances decline. It also projected that such a currency revaluation could knock 2 more percentage points off the economic growth rate, which is already expected to decline from 11 percent to 8 percent. The governor of the Central Bank, however, has denied Washington is demanding a 28-to-1 exchange rate. 25X1 25X1

Comment: Local businessmen have been openly critical of the government for pandering to US interests by allowing the currency to appreciate as much as it has. The government, sensitive to criticism at a time when President Chiang is moving ahead with political reforms, may have leaked the story, hoping the outcry from businessmen would allow it to resist additional US pressure by claiming the political liabilities are too great. 25X1

HONG KONG: Strong Economic Recovery

Hong Kong, bolstered by strong export growth, has reported a GDP growth of 8.7 percent for last year. Exports to Japan were up a sharp 32 percent. The territory's overall trade surplus with the US increased slightly to $5.2 billion—with exports up 9 percent. Hong Kong's overall trade account, however, was virtually in balance. 25X1

Comment: The territory will continue its strong opposition to adjusting its exchange rate to resolve the bilateral trade imbalance with the US for fear of eventually reviving downward speculative pressures on the Hong Kong dollar. Hong Kong's economic performance has been closely tied to the value of the US dollar since 1983, when the government linked the Hong Kong and US currencies in order to halt destabilizing speculation caused by the territory's uncertain future. The recent weakness of the US dollar—and hence the Hong Kong dollar—stimulated the territory's export-dominated economy. 25X1

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In Brief

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Americas [redacted] — **Bolivian** security has warned US Embassy that unemployed miners will march on La Paz this week . . . miners blame US for economic woes . . . may resort to violence. [redacted] 25X1

[redacted]

Middle East [redacted] — **Iranian** Foreign Minister on visit to **Sudan** . . . seeking to improve ties to Islamic regime there . . . Sudan wants to deal for oil, enhance its nonaligned credentials, discuss return of Sudanese POWs who fought for **Iraq**. [redacted] 25X1 25X1 25X1

— **North Yemen** has set up private firm to obtain Western military equipment, [redacted] . . may barter future oil revenues for arms . . . Sanaa still regards **USSR** as primary weapons supplier. [redacted] 25X1 25X1

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Special Analysis

ECUADOR: **Facing Hard Times**

The devastating impact of the recent earthquakes in the remote Amazon region of Ecuador on oil revenues and economic stability has placed the administration of President Febres-Cordero in a precarious position. The President will have to assert renewed leadership to keep the economy afloat and to deflect growing political pressure from leftist parties that seek to undermine his administration. Tensions between the armed forces and the leftist opposition may spark major confrontations that might lead the military either to shut down the congress or to provoke a showdown with Febres-Cordero. [redacted] 25X1 25X1

[redacted]

The earthquakes caused massive flooding and mudslides, killing several thousand people and leaving thousands more homeless. They destroyed at least 15 miles (24 kilometers) of Ecuador's main oil pipeline and damaged several pumping stations, forcing a shutdown of major oilfields. The country's petroleum exports could be suspended for six months or more, costing Ecuador more than $500 million in lost revenues. The total cost of the disaster, allowing for pipeline repairs, may exceed $950 million. These estimates may significantly underestimate the damage and the logistic problems of repair, however, because of the isolation of the affected region and the destruction of roads and bridges into the area. Ecuador's ability to produce oil may be affected because of damage to the oil reservoirs from the shutting down of the wells. [redacted] 25X1

[redacted] 25X1

Before the disaster, Ecuador was producing about 265,000 barrels of oil per day and exporting 180,000 barrels. [redacted] 25X1 25X1 25X1 Venezuela has already offered 83,000 b/d over the next two months to cover domestic needs and an additional 35,000 b/d over the next seven months to fulfill long-term contracts, according to sources of the US Embassy. Bogota has agreed to allow Ecuador to build an emergency link to its trans-Colombian pipeline with a capacity of 50,000 b/d; this would require at least two months to construct. [redacted] 25X1

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Outlook

Stabilizing the economic situation will test the political nerve of Febres-Cordero, who has maintained an uncharacteristically low profile since the Air Force mutiny two months ago. Unpopular austerity measures will almost certainly be necessary. [redacted] 25X1

The government will lose at least one-third of its anticipated tax revenues until oil production is restored. The US Embassy reports Febres-Cordero plans to increase gasoline prices by 80 percent, a move that will probably spark violent public protests and draw further criticism from opposition groups. [redacted] 25X1

[redacted] 25X1

Although Febres-Cordero has become increasingly dependent on the military in his frequent confrontations with the left, he now risks losing some military support, particularly if he is forced to make budget cuts. Moreover, fallout from cutting the military budget would probably strain his relations with key officers, currently the mainstays of his support. [redacted] 25X1

Yugoslavia: Indicators of Broader Instability

The following developments probably would be key warning signs of broader systemic instability:

- Public statements by Army leaders on the need for a crackdown on nationalists and dissidents.
- Serious attempts by party hardliners to purge liberals.
- Workers staging strikes across local boundaries or protesting political issues, not just work conditions.
- Serb-initiated ethnic violence against Albanians, pitting the Serb leadership against other nationalities.
- More open support by the Slovene leadership for attack on the system by a Slovene youth movement.

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Special Analysis

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YUGOSLAVIA: **Challenges to Stability**

Growing labor and ethnic problems are increasing the risk of disorders in Yugoslavia, although the security services and the decentralized political system will probably keep outbreaks localized. Meanwhile, the gradual erosion of central authority and weakening of political controls are encouraging increased openness that is beginning to approach Western standards in some regions. 25X1 25X1

Economic protest poses the greatest immediate danger to stability. New laws designed to curb consumer demand—including wage and price controls and credit restrictions—are meeting strong resistance from workers, leading to strikes last week that Yugoslav television called unprecedented. Wildcat strikes rose 50 percent last year to a record of about 900 nationwide. That figure is likely to rise if ~~Western~~ creditors require tougher austerity measures in coming debt talks.

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Ethnic tensions are also growing. ~~US diplomats report~~ Slovenia's tolerance of an iconoclastic, regionalist-minded youth movement is angering other regions. In the poorer south, the nationalistic press in Serbia is continuing its attacks against ethnic Albanians, despite efforts by the Serb leadership to tighten press controls. In Macedonia, ~~according to media reports~~ the authorities are risking flareups by purging Albanian officials and razing traditional stone walls around Albanian homes. 25X1 25X1

Forces of Order

The national political leadership has increasingly lost power, public confidence, and control over the pace of liberalization. The party has come to focus on procedural problems and cannot impose ideological conformity on liberal party members, especially in Slovenia and Serbia. Premier Mikulic's government has been unable to persuade the regions to implement federal tax and other laws adequately, a failure that disappoints Yugoslavs hoping for decisive action. 25X1

The regionally based security services, however, are prepared and probably able to put down any disturbances. Recently, Interior Minister Culafic publicly urged a crackdown on dissidents and nationalists. 25X1

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Army support is unlikely to be necessary to contain unrest nor is more direct military involvement in politics in the cards soon. The Army, long considered the country's principal unifying institution, now seems focused on protecting its economic prerogatives, and ethnic problems within the military are on the rise. Senior Army officials, however, have publicly demanded firmer action by the political leadership, 25X1

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Outlook

Local labor and ethnic unrest will increase this year, but regional rivalries make unlikely any nationwide disorder threatening the system. Unless the threat of instability rises sharply, however, the central authorities probably will be unable to reimpose the controls on the press and individual freedoms that existed under Tito. Without them, the country is likely to become even more open and pluralistic. 25X1

Moscow would probably use its limited influence to seek to preserve at least a veneer of central party control in Yugoslavia. It will watch Yugoslav developments closely in advance of the planned visit to Belgrade by General Secretary Gorbachev this summer. 25X1

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